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S E C R E T SECTION 01 OF 06 NOUAKCHOTT 000639

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SUBJECT: EXPANDING MINING OPERATIONS THREATENED BY THE COUP
AND BY TERRORISTS

Classified By: CDA Dennis Hankins for reasons 1.4 (b) and (d).

¶1. (C) Summary: EconOff recently visited SNIM's iron ore mining operations in northern Mauritania. After many years of low prices for iron ore, higher prices in recent years have led SNIM to develop new projects to increase production.

SNIM has two projects that it is developing on its own as well as three projects under development with foreign partners. SNIM is the largest importer of U.S. goods, purchasing nearly all of its heavy machinery and train locomotives from the United States. Because of the harsh environmental conditions in which SNIM operates, it continues to rely on old inefficient machines and equipment because many of the newer technologies are not suited for the conditions. Security and the threat of AQIM are a growing concern in Mauritania, but one that SNIM officials are reticent to talk about. AQIM ambushed Mauritanian soldiers on patrol just 30 km from SNIM's operations in September. SNIM officials assert that the company has enough independence from the government that the August 6 coup has not changed anything, but local press reports that SNIM's director general recently purchased a whole wardrobe of new suits for General Aziz. End Summary.

¶2. (U) EconOff recently visited the National Mining and Industrial Company's (SNIM) operations in the northern cities of Nouadhibou and Zouerate. SNIM was created as the result of the 1973 nationalization of the French mining company MIFERMA. SNIM, which is now 78% state-owned, has a monopoly on all iron ore mining operations in Mauritania. Mining is the backbone of the Mauritanian economy, and SNIM is the dominant actor in the sector. The mining sector consists primarily of iron ore mining carried out by SNIM, but gold, copper, and uranium mining have all begun recently. SNIM's earnings account for 12% of GDP, 45% of export earnings, and 8% of the national budget. It is also one of the country's largest employers.

¶3. (U) For many years, SNIM's production stagnated at about seven million tons of iron ore per year. Faced with low iron ore prices, SNIM was unable to expand production or increase investment. SNIM saw its fortunes start to improve around 2003 and 2004 when China could no longer produce enough iron ore domestically and began purchasing iron ore internationally. Increased demand from China caused global demand and prices to increase, which in turn improved SNIM's financial position and led it to increase production. SNIM currently operates three large mines and two small mines. It

will produce about 12 million tons of iron ore in 2008. Despite increased production, it is still a relatively small player in the iron ore market. The market is dominated by three companies (Vale, BHP Billiton, and Rio Tinto Group), which combined produce approximately 700 million tons of iron ore per year. SNIM has traditionally sold all of its production to European customers, but after signing two new agreements with Chinese companies in 2007, it will sell 20% of its production to China in 2008.

¶4. (U) In 2005 SNIM developed a new strategy to address the changing economic conditions and greater demand for iron ore.

Due to the long lead time for new mines to come into production and the long life span of the mines, SNIM's development plans look at least 20 to 30 years out.

Development for its large mines takes at least 10 years from the time development begins until iron ore production begins.

Because all of SNIM's investments are for the long-term, it is taking a cautious approach in the case that the current high prices are not sustained. After suffering many years of low prices for iron ore, SNIM officials are well aware of what the future could bring. The head of mining operations Mohamed Ould Mohamed Abdallahi told EconOff that recent global economic problems will not change SNIM's long-term development plans.

¶5. (U) In its 2005 development plan, SNIM identified new projects that it will develop and finance itself as well as projects that it will realize in conjunction with foreign partners. Through its self-developed and financed projects, SNIM intends to increase production to 18 million tons per

NOUAKCHOTT 00000639 002 OF 006

year by 2012. To do so, SNIM has begun adding new equipment to a deposit that is already being exploited in order to increase production by two million tons per year by 2010. It is also planning to build a new concentration factory, which will produce an additional four million tons per year by **¶2012**. A Canadian company has already completed the feasibility study for the concentration factory. SNIM is now looking for financing from development and commercial banks to fund the 500 million Euro project.

¶6. (U) SNIM also has three projects that are under development with foreign partners. This first is a project that it began with the Australian company Sphere in 2005 to begin producing iron ore pellets, which have extremely high iron ore content (71%) and sell for approximately twice the price of regular iron ore. The project will initially produce seven million tons of pellets per year, but will have the capacity to expand to 28 million tons per year. The project is estimated to cost \$2 billion. However, the project is currently stalled due to a lack of financing. Saudi Basic Industries Corporation (SABIC) was one of the original investors but it pulled out in 2007. SABIC was replaced by Qatar Steel, which subsequently pulled out of the project in August, citing concerns about the profitability of the project. In September, SNIM and Sphere appointed USB to help them identify a strategic partner for the project, which would hold a 49.9% share in it.

¶7. (U) ArcelorMittal signed an agreement with SNIM in December 2007 to jointly develop a new iron ore mining project. ArcelorMittal is one of SNIM's traditional partners, but as a buyer, not a developer. The project is still at the beginning stages and ArcelorMittal must create a subsidiary for the new joint venture company that it will form with SNIM before work can actually begin. The project is still years away from coming into production. A feasibility study must first be done, which is expected to take three years. ArcelorMittal currently holds a 30% share in the project. If the results of the feasibility study are positive, then the two partners will begin developing the site and ArcelorMittal will have the option to take a 70% stake in the project. The project could produce up to 25 million tons per year. The site where they are intending to

develop the project is 30 km away from the existing railway, meaning that a railway extension will also be necessary.

¶ 18. (SBU) The Chinese have been active in developing new projects in conjunction with SNIM since March. They are currently exploring the possibility of developing underground mines at sites that have already closed. Many of these mines still contain iron ore, but it is underground. Because these projects are still at the early stages, they have not released production estimates. It is relatively rare to mine for iron ore underground. Given that there is not significant international experience in underground iron ore mining and the relatively lax safety regulations in Mauritania, the new underground mining projects could pose a safety concern.

¶ 19. (C) To handle increased production, SNIM will have to expand its infrastructure. It will extend the current 700 km railway to several new sites as iron ore production comes on line. It will also increase the number of trains that run each day from three to six. In addition, SNIM has plans to build a new port facility in the northern city of Nouadhibou.

Its current port facility in Nouadhibou is aging and cannot accommodate many of the new larger ships. According to plans, the new port which will be adjacent to the current port should be operational by 2012. Even after the new port is completed, SNIM plans to maintain the old port as a back-up and potentially for regular use as production continues to increase. The most significant hurdle facing the new port is funding. It is expected to cost 116 million euros to build. The European Union had agreed to provide 40 million euros for the project, but it has frozen that money since the August 6 coup. If the coup is overturned, SNIM will likely receive the money as planned. If the coup is not overturned and the European Union implements sanctions in Mauritania, it could present a significant hurdle to

NOUAKCHOTT 00000639 003 OF 006

completing the construction of the new port.

¶ 110. (U) SNIM has spoken of the possibility of eventually expanding into steel production, but it is more of a dream than a reality at this point. The only way for steel production to become viable in Mauritania is if coal or gas to provide sufficient energy is found. Gas could be a viable possibility in the future as initial surveys indicate that there could be substantial gas deposits offshore. Further testing and studies are still needed to determine if gas production could be commercially viable in Mauritania. If gas production is proven to be viable, it would still require significant time and money before steel production could ever begin in Mauritania.

¶ 111. (U) A visit to the SNIM facilities is like a time warp back to the 1960s. SNIM continues to use and rely on almost all of the original equipment and facilities that were built in the 1950s and 1960s by the French company MIFERMA that originally began mining in Mauritania. Because of the long period of stagnation in the iron ore market, SNIM did not have capital for investment and renewing its equipment. In addition, the extreme heat, sand, dust, and lack of water in Mauritania makes it a uniquely challenging environment for iron ore mining. Most of the heavy equipment and machinery that SNIM uses is specially made or adapted for the conditions. The equipment and technologies used by other mining companies simply would not work in the harsh conditions in Mauritania. Because water is very limited in northern Mauritania, SNIM uses specially adapted equipment that uses very little water, but as a result is extremely energy intensive. Much of the newer equipment is much more energy efficient, but would not work in the local conditions. As a result, SNIM continues to use the same old equipment that was specially developed for it in the 1950s and 1960s because it has little alternative.

¶ 112. (U) SNIM will spend \$105 million on new equipment in 2008

and it is the largest Mauritanian buyer of U.S. goods. SNIM purchases nearly all of its mining equipment (large trucks, loading machines, electric shovels, digging and drilling equipment, and bulldozers) from the United States, primarily from Caterpillar, Bucyrus, and P&H. It also purchases all of its locomotives from GM's Electro-Motive Division. It currently has 21 locomotives and recently purchased eight additional ones. The first two new locomotives will arrive by 2010 to increase annual production to 14 million tons per year and the remaining six will arrive by 2011 to increase production to 18 million tons per year. Director of Operational Production Mohamed Khalifa Ould Beyah said that SNIM originally used locomotives produced by a French company, but they were not able to withstand Mauritania's harsh environment and constantly broke down. SNIM replaced all of the French locomotives with GM locomotives specially adapted for use in Mauritania. He said that the GM locomotives have performed extremely well and many of the original locomotives are still in use. In the coming months SNIM intends to put out a bid for eight additional locomotives to retire some of its oldest ones. The bid will be open to all companies, but SNIM intends to purchase them from GM because of its proven track record and the need for standardization in the fleet to keep maintenance and operating costs down. Because Mauritania is so far from its suppliers, obtaining parts is difficult and time consuming. There is a six to twelve month delay between the time a part is ordered and the time it is delivered. This means that SNIM has to maintain stocks of parts and supplies for at least seven months. With over 95,000 different parts in use, keeping new parts to a minimum is important.

¶13. (S) Security is an increasingly important concern in Mauritania. After four terrorist attacks in Mauritania in the past twelve months, there is growing awareness of the threat posed by AQIM. In September, a group of Mauritanian soldiers out on patrol were ambushed near the town of Tourine, just 30 km from SNIM's mining operations in Zouerate. There is speculation that SNIM was AQIM's intended target. SNIM officials that EconOff spoke with were quick to reassure that security was under control to try to establish

NOUAKCHOTT 00000639 004 OF 006

confidence in their operations. Most dismissed the recent attack in Tourine as an isolated incident. While saying that they were not concerned, actions taken by SNIM officials during EconOff's visit clearly indicated that they were nervous. EconOff traveled on SNIM's iron ore train 700 km from Nouadhibou to Zouerate. Normally the train takes other passengers during the trip, but SNIM officials refused to let any passengers other than Embassy personnel on board. The train normally makes seven to eight stops along the way, but the train only made two stops: one to let another train pass and another to change conductors at the midway point. EconOff also had armed plain clothes police officers outside of her hotel room at all times. Local residents of Zouerate told Embassy FSNs that they had created the equivalent of a neighborhood watch following the attack in Tourine. Stating that they did not trust the military and police forces to be able to provide security, they thought that it was necessary to take matters into their own hands and were watching anyone who did not belong.

¶14. (S) SNIM would present an inviting and ready target for AQIM. Because revenues from iron ore mining make up such an important part of the national budget and GDP and because mining is such an important part of Mauritanian national identity, an attack on SNIM could cripple the country and the economy. SNIM could be a relatively easy target. Its operations are located in northern Mauritania, a vast no man's land. Operations are spread out over a relatively large area and have little in the way of lighting, fencing, or guards. SNIM officials said that they had recently taken measures to step up security, but if they have, they are not visible. For example, hundreds of large bags of nitrogen used for explosives were clearly visible sitting outside

unsecured. The only thing separating them from the main road 100 feet away was a chain link fence with no barbed wire. The train, which runs along a nearly 700 km track, is largely unprotected. An attack on the railroad would bring mining operations to a halt in the short-term until repairs could be made, but would be much more damaging in the long-term by creating a climate of fear, leading customers to reconsider their long-term contracts with SNIM for fear that they would not be fulfilled and investors to reconsider the feasibility of making a major investment in the region. In a poor country without a diversified economy, Mauritania is heavily reliant on iron ore mining to support the economy and government operations. A downturn in SNIM's production as a result of an AQIM attack would devastate Mauritania's economy, especially in the current context where a lot of donor money has been frozen since the coup.

¶15. (C) SNIM officials that EconOff spoke with were quick to distance the company from the government and the military junta. All were unanimous in asserting that nothing had changed in terms of SNIM's operations since the coup. Although the state holds a 78% share, SNIM operates as an independent company. SNIM officials explained that there is a convention governing the relationship between SNIM and the government, which essentially protects SNIM from government interference. They also added that the vast majority of SNIM's accounts are held in Europe, not Mauritania, which gives them some measure of protection from the junta. However, if the junta's financial situation continues to worsen with the freezing of donor aid, it could always look to SNIM as a source of hundreds of millions of dollars to buoy its position. Comment: SNIM may certainly have reason to believe that things will continue for the company post-coup the same as they were pre-coup given the number of coups and governments that the company has weathered in its 35 year history. On the other hand, things may be different this time, especially as the company is an expansionary phase. The EU has already frozen the money it had promised for SNIM's new port facility. Foreign investors and banks may be less inclined to invest in SNIM given the opaque political situation, especially during the current economic crisis. End Comment.

¶16. (C) The Mauritanian press reports that SNIM Director General Mohamed Ould Sidi Mohamed Deyahi recently purchased a whole new wardrobe of suits for General Aziz and brought his

NOUAKCHOTT 00000639 005 OF 006

personal tailor down from Morocco. Deyahi reportedly said that General Aziz looked too much like a "mafioso" in his usual cheap polyester suits. Post can neither confirm nor deny this report, but post LES believe the report to be true.

They say that it is a tradition in Mauritania to purchase gifts for one's boss to garner favor and keep one's job. Deyahi is reported to be very close to both the military junta and the businessmen who are actively supporting the coup -- although he had called Charge in the past to emphasize he is just a businessman with no connection to the regime.. Deyahi was originally appointed director general of SNIM by the last military junta, the CMJD. There is ample reason to believe that he might have believed that his job was at risk. The junta has recently replaced the directors of almost all state owned companies, including the Port of Nouakchott, the Port of Nouadhibou, SOMELEC (electricity company), and SONIMEX (national import-export company) among others. Deyahi likely feared that he would be the next to go or that the junta would open a potentially embarrassing corruption investigation into his tenure as the director general of SNIM. Comment: Deyahi and his son Sidi Mohamed Mohamed Aly Deyahi both applied for visas to travel to the United States in the past week. Post has referred their cases to the Department with the recommendation that they be denied given Deyahi's apparent active support of the junta. End Comment.

¶17. (C) EconOff also met with the mayor of Zouerate Yacoub

Ould Salem Vall. Vall, the first Afro Mauritanian mayor of Zouerate, is a member of Messaoud Ould Boulkheir's APP party and is strongly anti-coup. He stated that he has "no need" for the governor (wali) or prefect (hakem) of the region. He stated that he did not find them to be helpful and limits contact with them to the extent possible, only going to seem them when ordered to do so. Even as a SNIM employee, Vall was much more open and willing to discuss the impact of the coup and security on SNIM's operations than were other higher ranking SNIM employees. He stated that while SNIM was creating a security strategy and had already taken some modest measures such as adding barbed wire, much still needs to be done to change people's mentality about the importance of security. Vall added that SNIM relies on foreigners to come in regularly to perform certain maintenance operations, but many had refused to come since the attack in Tourine because of security concerns. Vall also said that even many residents of Zouerate were scared. He said that he routinely travels overland from Zouerate when he has business to attend to in Nouakchott. When friends and neighbors heard that he was intending to drive to Nouakchott just days after the Tourine ambush, he said that many people approached him and told him not to do so because it was not safe.

¶18. (C) Vall lamented that Zouerate has fallen into a virtual "black hole" of development and that the city has become a victim of infighting between the central government and SNIM.

The central government contends that it does not have to provide financial resources to Zouerate because SNIM will take care of the town. SNIM responds that it is a for-profit company, not a charitable organization. It already gives nearly all of its dividends to the central government; therefore the government should provide money for development to Zouerate just like it does to other towns. Caught in the middle, Zouerate receives almost nothing. What work has been done recently such as the paving of new roads and refurbishing of schools was paid for primarily by the World Bank. In addition, as Vall is strongly opposed to the coup, whatever money that Zouerate was getting from the central government has now been terminated. Vall also said that Zouerate is faced with additional difficulties because SNIM is exonerated from paying local taxes, which has led to a battle between SNIM, the central government, and the city of Zouerate. Zouerate says that SNIM owes it 1.5 billion ouguiya (\$5.75 million) in property taxes for the past two years. The city's annual budget, including money for development projects, is less than \$400,000. SNIM normally contributes about \$17,000 per year. Vall said that the city of Zouerate had reached an agreement with SNIM where it will pay a little over \$1 million to the city this year. The agreement is far less than what the city claims SNIM owes it,

NOUAKCHOTT 00000639 006 OF 006

but it is nonetheless a significant increase compared to previous years.

¶19. (U) Vall said that environmental problems are plaguing Zouerate. There are severe water shortages in much of Mauritania, but particularly in the north. He said that a lot of research has been done into the water situation, but there has never been any coordination between the Ministry of Hydrology, the Ministry of Mines, and SNIM. As a result, the problem has never been solved. He also said that a Moroccan firm had conducted a study into the feasibility of recycling waste water, but the city had never been able to find a donor to fund a waste water treatment plant. Vall noted with irony that SNIM had always managed to locate new water resources for each new mine that it wanted to develop, but that it had never been able to do so for the city. In addition to the water shortages plaguing the town, Vall said that he believes that there are high levels of contaminants and toxins in the air and water as a result of the mining activities. He said that he does not have the tools to be able to measure them, but from anecdotal evidence, he believes that they must exist. He said that a large proportion of the town's residents are sick, but their symptoms cannot be explained.

120. (C) Comment: SNIM is at a turning point in its history and has the opportunity to substantially increase production and profits. With record demand and prices for iron ore, it is well poised for the future. However, there are questions as to whether SNIM will be able to fully execute its development plans. First and foremost, financing is critical for several of its new projects, and there is no guarantee that it will fall into place, especially given the current economic uncertainty. If current economic conditions continue, it could drive the price of iron ore back down again, essentially shutting down new development. The current political situation in Mauritania is also a potential problem. In the short term financing for the new port is at risk. In the longer term buyers and investors could start to look elsewhere if sanctions are implemented. In addition, looking for short-term gain, the junta could drain SNIM's resources, destroying one of the country's most important resources in the long-term. Finally, security will be an ongoing challenge. While nobody wants to acknowledge it, investors are unlikely to invest in Mauritania if there is not same degree of security. SNIM has weathered many storms and will likely weather new ones that come its way, but some may impede its ability to fulfill its potential. End comment.

HANKINS